

**CITY OF NATIONAL CITY
NATIONAL CITY, CALIFORNIA**

Single Audit Report on Federal Awards

Year ended June 30, 2005

CITY OF NATIONAL CITY
Single Audit Report on Federal Awards
Year ended June 30, 2005

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Honorable Members of the City Council
City of National City, California

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED
ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

We have audited the financial statements of the City of National City, California, as of and for the year ended June 30, 2005, and have issued our report thereon dated December 21, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of National City's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the City of National City's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the accompanying schedule of findings as item 05-01.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we considered the reportable condition described above as item 05-01 to be a material weakness. We also noted other immaterial matters involving internal control over financial reporting which we have reported to management in a separate letter dated December 21, 2005.

Honorable Members of the City Council
City of National City, California
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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of National City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial instances of noncompliance, which we have reported to management in a separate letter dated December 21, 2005.

This report is intended solely for the information and use of the City's management and City Council and is not intended to be and should not be used by anyone other than these specified parties.

Conrad and Associates, L.L.P.
December 21, 2005

Honorable Members of the City Council
City of National City, California

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO
EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL
AWARDS IN ACCORDANCE WITH OMB CIRCULAR A-133**

Compliance

We have audited the compliance of the City of National City, California, with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2005. The City of National City's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City of National City's management. Our responsibility is to express an opinion on the City of National City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of National City, California's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of National City's compliance with those requirements.

In our opinion, the City of National City complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2005.

Internal Control Over Compliance

The management of the City of National City is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City of National City's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards and Financial Data Schedule

We have audited the basic financial statements of the City of National City as of and for the year ended June 30, 2005, and have issued our report thereon dated December 21, 2005. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards and Financial Data Schedule are presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended for the information of the City's management, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than those specified parties.

Conrad and Associates, L.L.P.

December 21, 2005

CITY OF NATIONAL CITY
Schedule of Expenditures of Federal Awards
Year ended June 30, 2005

Federal Grantor/ Pass-through Grantor/ <u>Program Title</u>	Program Identification <u>Number</u>	Federal Domestic Assistance <u>Number</u>	Federal Financial Assistance <u>Expenditures</u>
<u>U.S. Department of Health and Human Services</u>			
Passed through the County of San Diego:			
Special Programs for the Aging, Title III, Part C	388636	93.045	\$ 375,291
<u>U.S. Department of Housing and Urban Development</u>			
Direct assistance:			
Community Development Block Grant - Entitlement Program	B-02-MC-06-0560	14.218	1,324,000
Home Program - Entitlement Program	M-02-MC-06-0522	14.239	666,000
Section 8 Housing Choice Vouchers	CA116V0	14.871	8,307,060 *
Section 8 Housing Choice - Morgan Towers**	CA60006011	14.871	498,690 *
Supportive Housing for the Elderly - Morgan Towers	CA60006011	14.157	3,328,141 *
Lead Hazard Control Grant	CALHB0238-03	14.900	694,326
Total U.S. Department of Housing and Urban Development			14,818,217
<u>U.S. Department of Justice</u>			
Direct assistance:			
Local Law Enforcement Block Grant	2004LBBX1137	16.592	32,057
COPS in Schools	2002SHWX0152	16.710	20,162
Passed through the State of California Office of Criminal Justice Planning:			
Jurisdictions United for Drug Gang Enforcement Program	DC02150370	16.581	53,829
Total U.S. Department of Justice			106,048
<u>U.S. Department of Transportation</u>			
Passed through State of California Department of Transportation:			
Highway Bridge Rehabilitation	5066 (004)	20.205	5,837
Total U.S. Department of Transportation			5,837
<u>Executive Office of the President - Office of National Drug Control Policy</u>			
Passed through the City of San Diego Police Department:			
High Intensity Drug Trafficking Areas	I8PSCP55	N/A	65,731
<u>Federal Bureau of Investigation</u>			
Passed through the San Diego County Regional Auto Theft Task Force:			
RATT Overtime	N/A	N/A	53,761
Total Federal Financial Assistance Expenditures			\$ 15,424,885

* Major Program

** See Note 1(d) in the Notes to the Schedule of Federal Awards for HUD required information.

The accompanying notes are an integral part of this schedule.

CITY OF NATIONAL CITY, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards

Year ended June 30, 2005

(1) Summary of Significant Accounting Policies Applicable to the Schedule of Expenditures of Federal Awards

(a) Scope of Presentation

The accompanying schedule presents only the expenditures incurred (and related awards received) by the City of National City, California (City) which are reimbursable under federal programs of federal financial assistance. For purposes of this schedule, federal awards include both federal financial assistance received directly from a federal agency, as well as federal funds received indirectly by the City from non-federal organizations. Only the portion of program expenditures reimbursable with such federal funds are reported in the accompanying schedule. Program expenditures in excess of the maximum federal reimbursement authorized and the portion of program expenditures that were funded with state, local or other non-federal funds are excluded from the accompanying schedule.

(b) Basis of Accounting

The expenditures included in the accompanying schedule were reported on the modified accrual basis of accounting. Under the modified accrual basis of accounting, expenditures are recognized when the City becomes obligated for payment as a result of the receipt of the related goods and services. Expenditures reported include any property or equipment acquisitions incurred under the Federal program.

(c) Subrecipients

There were no payments to subrecipients for the year ended June 30, 2005.

(d) Supplementary Information Required by HUD – Financial Data Schedule

The *financial data schedule* supplementary information required by the U.S. Department of Housing and Urban Development (HUD) for the Morgan Towers Section 8 Housing Choice Voucher program is reported in a separate report entitled "Morgan Towers Financial Statements and Single Audit Report for the year ended June 30, 2005", dated September 8, 2005. These financial statements may be obtained from the Community Development Commission of the City of National City located at 140 East 12th Street, Suite B, National City, CA 91950.

CITY OF NATIONAL CITY
Financial Data Schedule
June 30, 2005

Section 8
Housing
Assistance

Assets

Current assets:	
Cash and investments	\$ 651,567
Total current assets	<u>651,567</u>
Non-current assets:	
Prepaid items and deposits	<u>3,386</u>
Total non-current assets	<u>3,386</u>
Total assets	<u>\$ 654,953</u>

Liabilities and Fund Balance

Current liabilities:	
Accounts payable and accrued liabilities	\$ 197,210
Due to other funds	<u>1,210,146</u>
Total current liabilities	<u>1,407,356</u>
Total liabilities	<u>1,407,356</u>
Fund balance:	
Undesignated fund balance	<u>(752,403)</u>
Total liabilities and fund balance	<u>\$ 654,953</u>

Revenues:	
Housing assistance voucher program	\$ 8,307,062
Miscellaneous revenue	4,418
Investment income	<u>37,587</u>
Total revenues	<u>8,349,067</u>

Expenditures:	
Administrative	688,132
Special services	218,028
Operating and maintenance expenditures	258,970
Housing assistance payments	<u>7,162,357</u>
Total expenditures	<u>8,327,487</u>
Excess (deficiency) of revenues over (under) expenditures	<u>21,580</u>

Other financing sources (uses):	
Transfer out	<u>(1,165,471)</u>
Total other financing sources (uses)	<u>(1,165,471)</u>
Net change in fund balance	<u>(1,143,891)</u>
Beginning fund balance	<u>391,488</u>
Ending fund balance	<u>\$ (752,403)</u>

CITY OF NATIONAL CITY, CALIFORNIA

Schedule of Findings and Questioned Costs

Year ended June 30, 2005

(A) Summary of Auditors' Results

1. An unqualified report was issued by the auditors on the financial statements of the auditee.
2. There was one reportable condition in internal control over financial reporting that we described as item (05-1) below. We considered this reportable condition to be a material weakness. We also noted other immaterial matters over internal control over financial reporting that we have reported to the management of the City of National City, California in a separate letter dated December 21, 2005.
3. The audit disclosed no instance of noncompliance that was material to the financial statements of the auditee. However, we noted other immaterial matters of noncompliance that we have reported to the management of the City of National City in a separate letter dated December 21, 2005.
4. There were no material weaknesses or other reportable conditions in internal control over the major programs of the auditee.
5. An unqualified report was issued by the auditors on compliance for major programs.
6. The audit disclosed no audit findings over federal awards required by the auditors to be reported under paragraph .510(a) of OMB Circular A-133.
7. The major programs of the auditee were the Section 8 Housing Assistance Payment Program – Voucher Program, CFDA #14.871 and Supportive Housing for the Elderly, CFDA #14.157.
8. The dollar threshold used to distinguish Type A and Type B programs was \$462,747.
9. The auditee was not considered to be a low risk auditee for the year ended June 30, 2005 for the purposes of determining major programs.

(B) Findings Related to the Financial Statements which are Required to be Reported in Accordance with GAGAS

(05-01) Inadequate Internal Controls over Cash and Investments

During our review of internal controls over cash and investments, we noted that the cash and investment portfolios for the Community Development Commission (CDC) (including cash and investments held by their respective fiscal agent) had not been reconciled to the general ledger in a timely manner requiring certain unsupported adjustments to be made at year end in order for cash and investments to balance to the general ledger. Sound internal controls dictate that the individuals in charge of reconciling the investment portfolios to the general ledger ensure that all cash and investment activities (i.e., purchases, sales, transfers, interest earnings)

CITY OF NATIONAL CITY, CALIFORNIA

Schedule of Findings and Questioned Costs

(Continued)

(B) Findings Related to the Financial Statements which are Required to be Reported in Accordance with GAGAS, (Continued)

(05-01) Inadequate Internal Controls over Cash and Investments, (Continued)

have been accurately and timely recorded in the general ledger. This monthly procedure should be done soon after month end in order to efficiently detect and resolve any discrepancies or unauthorized transactions that might occur.

Recommendation

We recommend that the CDC use the original monthly investment statements received directly from the various financial institutions to reconcile and record all cash and investment activity to the general ledger on a regular monthly basis. We further recommend that the City and CDC consider the use of a third party custodian in performing investment transactions for all investments held. The involvement of a third party custodian (separate and distinct from the institution that executes the investment purchase on the City and CDC's behalf) enhances the internal controls over investments by decreasing the risk of fraud by the counter party, the party that makes the investment purchase.

Management Response

Since the completion of the audit, the responsibility of reconciliation of cash and investments has been assigned to a staff member and will be completed within 45 days of the month end. Should these reconciliations not be completed within a timely manner, a written explanation will be provided to the Finance Director. Furthermore, these reconciliations will be reviewed by another to ensure timely and accurate recordings. With the merger of the CDC with the City of National City, the costs and benefits of obtaining a third party custodian in performing investment transactions for both the CDC and the City will be considered by the Investment Committee.

(C) Findings and Questioned Costs for Federal Awards as Defined in Paragraph .510(a) at OMB Circular A-133

There are no auditors' findings to be reported in accordance with paragraph .510(a) at OMB Circular A-133.

CITY OF NATIONAL CITY, CALIFORNIA

Summary Schedule of Prior Audit Findings

Year ended June 30, 2005

The following are the status of the audit findings for the year ended June 30, 2004:

04-1 Inadequate Internal Controls over Cash and Investments

Matter was not resolved and therefore was repeated as an audit finding in the current year.

04-02 Internal Control over Payroll

Matter was resolved. The City implemented the recommendation that changes to the payroll master file be performed by a person independent of the payroll process.

This report is solely intended for the information and use of the management, City Council and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

January 26, 2005

